



# International procurement, development bank procurement and FIDIC

## Introduction

1. The purpose of this paper is to discuss certain issues relevant to international procurement by reference to the FIDIC form of contract and the approach of the World Bank to procurement and the FIDIC form of contract.
2. More specifically, this paper is set out in the following sections:
  - (i) The FIDIC form: a brief history;
  - (ii) The MDB version of the new Red Book May 2006; and
  - (iii) World Bank procurement;

## The FIDIC form: a brief history

3. The FIDIC organisation was founded in 1913 by France, Belgium and Switzerland. The UK did not join until 1949. The first edition of the *Conditions of Contract (International) for Works of Civil Engineering Construction* was published in August 1957 having been prepared on behalf of the Fédération Internationale des Ingénieurs-Conseils (FIDIC) and the Fédération Internationale des Bâtiment et des Travaux Publics (FIBTP).<sup>1</sup>
4. The form of the early FIDIC contracts followed closely the fourth edition of the ICE Conditions of contract. In fact so closely did the FIDIC form mirror its English counterpart that Ian Duncan Wallace commented that:

*“as a general comment, it is difficult to escape the conclusion that at least one primary object in preparing the present international contract was to depart as little as humanly possible from the English conditions”.*<sup>2</sup>
5. One difficulty with the original FIDIC Red Book was that it was based on the detailed design being provided to the contractor by the employer or his engineer. It was therefore best suited for civil engineering and infrastructure projects such as roads, bridges, dams, tunnels and water and sewage facilities. It was not so suited for contracts where major items of plant were manufactured away from site. This led to the first edition of the “Yellow Book” being produced in 1963 by FIDIC for mechanical and electrical works. This had an emphasis on testing and commissioning and so was more suitable for the manufacture and installation of plant. The second edition was published in 1980.
6. Both the Red and Yellow Books were revised by FIDIC and new editions published in 1987. A key feature of the 4th edition of the Red Book was the introduction of an express term which required the engineer to act impartially when giving a decision or taking any action which might affect the rights and obligations of the parties, whereas the previous editions had assumed this implicitly.

<sup>1</sup> Gradually, further sponsors were added including the International Federation of Asian and West Pacific Contractors Associations, the Associated General Contractors of America, and the Inter-American Federation of the construction industry.

<sup>2</sup> I.N. Duncan Wallace QC, *The International Civil Engineering Contract*, 1974.

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7. A supplement was published in November 1996 which provided the user with the ability to incorporate alternative arrangements comprising an option for a Dispute Adjudication Board to go with modelled terms of appointment and procedural rules, and an option for payment on a lump sum basis rather than by reference to bills of quantities.
  8. In 1995 a further contract was published (known as the Orange Book). This was for use on projects procured on a design and build or turnkey basis, dispensing with the engineer entirely, and provided for an “Employer’s Representative”, who, when determining value, costs or extensions of time, had to:

*“determine the matter fairly, reasonably and in accordance with the Contract”.*
  9. Consequently the need to submit matters to the engineer for his “Decision” prior to an ability to pursue a dispute, was eliminated. In its place an Independent Dispute Adjudication Board was introduced consisting of either one or three members appointed jointly by the employer and the contractor at the commencement of the contract, with the cost being shared by the parties. This provision mirrored a World Bank amendment to the FIDIC Red Book.
  10. Although this talk concentrates on the new FIDIC forms, it should be remembered that the FIDIC 4th edition 1987 (“The Old Red Book”) remains the contract of choice throughout much of the Middle East, particularly the UAE. However, this may soon change, as the government in Abu Dhabi introduced its own version of the 1999 FIDIC Red Book under cover of Law 21 of 2006. The Conditions, known as the Abu Dhabi Government Conditions of Contract which apply only to government and not private contracts, came into force in September 2007.

## The new FIDIC forms 1999

11. In 1994 FIDIC established a task force to update both the Red and the Yellow Books in the light of developments in the international construction industry, including the development of the Orange Book. The key considerations included:
    - (i) The role of the engineer and in particular the requirement to act impartially in the circumstances of being employed and paid by the employer.
    - (ii) The desirability for the standardisation of the FIDIC forms.
    - (iii) The simplification of the FIDIC forms in light of the fact that the FIDIC conditions were promulgated in English but in very many instances were being utilised by those whose language background was other than English.
    - (iv) The new books would be suitable for use in both common law and civil law jurisdictions.
  12. This led to the publication of four new contracts in 1999:
    - (i) Conditions of Contract for Construction for Building and Engineering Works Designed by the Employer: The Construction Contract (the new Red Book);
    - (ii) Conditions of Contract for Plant and Design-Build for Electrical and Mechanical Plant and for Building and Engineering Works, Designed
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- by the Contractor: The Plant and Design/Build Contract (the new Yellow Book);
- (iii) Conditions of Contract for EPC/Turnkey Projects: the EPC Turnkey Contract (the Silver Book);
- (iv) A short form of contract (the Green Book).
13. In keeping with the desire for standardisation, each of the new books includes General Conditions together with guidance for the preparation of the Particular Conditions, and a Letter of Tender, Contract Agreement and Dispute Adjudication Agreements. Whilst the Red Book refers to works designed by the employer, this reflects the main responsibility for design and it is appropriate where the works include some contractor designed works whether civil, mechanical, electrical or construction work.
14. FIDIC is also aware of the need to develop new contract forms in order to adapt to changing conditions. On 13 September 2007, in Singapore, FIDIC launched their new DBO<sup>3</sup> form of contract. The DBO form is a response to the call for a standard concession contract for the transport and water/waste sectors. The market currently uses the existing FIDIC Yellow Book with operations and maintenance obligations tacked on. FIDIC recognised this unsatisfactory state of affairs and the need to tailor a form to meet the demand.

## The content of the new FIDIC forms

15. The new FIDIC form has 20 clauses which are perhaps best viewed as chapters covering the key project topics. I propose to consider some of the more important ones.
16. Clause 2 addresses the role of the employer. There are two particularly interesting sub-clauses. First sub-clause 2.4 renders it mandatory upon the employer following request from the contractor to submit:
- reasonable evidence that financial arrangements have been made and are being maintained which will enable the employer to pay the contract price punctually...; [and]
- Before the employer makes any material change to his financial arrangements, the employer shall give notice to the contractor with detailed particulars.
17. Failure to submit such evidence provides the Contractor with the entitlement to suspend work, “*or reduce the rate of work*”, unless and until the contractor has received the reasonable evidence. This was an entirely new provision to the 1999 FIDIC form and provides a mechanism whereby the Contractor can obtain confirmation that sufficient funding arrangements are in place to enable him to be paid, including if there is a significant change in the size of the project during construction.
18. Second, sub-clause 2.5 requires the Employer to give notice and particulars to a Contractor:
- “if the employer considers himself to be entitled to any payment under any clause of these conditions or otherwise in connection with the Contract”.*
19. Clause 3 deals with the position of the Engineer. There has been a significant change from the 1987 edition. The express reference in the 1987 edition to the Engineer’s impartiality has gone. Unless otherwise stated:

3 DBO meaning design-build operate

*“Whenever carrying out duties or exercising authority, specified in or implied*

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*by the Contract, the Engineer shall be deemed to act for the Employer.”*

Now, the conditions provide that the Engineer shall proceed in accordance with sub-clause 3.5 to agree or determine any matter:

*the Engineer shall consult with each Party in an endeavour to reach agreement. If agreement is not achieved, the engineer shall make a fair determination in accordance with the Contract, taking due regard of all relevant circumstances.*

20. Clause 4 is by far the longest sub-clause and covers the Contractor’s general obligations including the requirement that in respect of Contractor designed works:<sup>4</sup>

*“it shall, when the works are completed, be fit for such purposes for which the part is intended as are specified in the Contract”.*

21. This is an absolute duty.

22. Sub-clause 4.2 specifies that the Contractor shall provide a performance security<sup>5</sup> where the amount has been specified in the Appendix to Tender, and the sub-clause continues with provisions for extending the security. Some protection is afforded to the Contractor as the sub-clause includes an indemnity by the Employer in favour of the Contractor against damage, loss and expense resulting from a claim under the performance security:

*“to the extent to which the Employer was not entitled to make the claim”.*

23. The Employer ought to have reached a decision on what document it requires to comprise the performance security and its wording at the stage of the preparation of tender documentation. Whilst the Old Red Book favoured bonds which were in conditional terms, payable upon default, there has been a trend towards the use of first or on-demand bonds.<sup>6</sup> This is reflected in the 1999 form where the performance guarantees are in an on-demand guarantee form, which is payable upon the submission of identified documentation by the beneficiary. It is necessary to state in what respect the Contractor is in breach of his obligations. In keeping with the intentions of FIDIC to achieve a degree of uniformity and hence clarity, the securities derive from the guidance of the International Chamber of Commerce and the Uniform Rules published by that body.<sup>7</sup>

24. Clause 4.21 provides details of the information required to be inserted by the Contractor in the Progress Reports. The provision of this report is a condition of payment. Under clause 14.3, payment will only be made within 28 days of receipt of the application for payment and the supporting documents, one of which is the Progress Report.

25. Whilst the importance of ensuring that the Progress Reports are accurate might seem obvious, His Honour Judge Wilcox, in a recent case<sup>8</sup> involving a construction manager, highlighted some of the potential difficulties where that reporting is not accurate.

26. Under the terms of the particular contract, the construction manager was described as being the only person on the project with access to all of the information and the various programmes. He was the only available person who could make an accurate report to the client at any one time, of both the current status of the project and the likely effects on both timing and costs. He was at *“the centre of the information hub”* of the project.

<sup>4</sup> Obviously, the reference to design changes throughout the various FIDIC forms.

<sup>5</sup> The FIDIC form has a number of sample forms of security.

<sup>6</sup> See Lord Denning in *Edward Owen Engineering Ltd v Barclays Bank International Ltd and Umma Bank (1978)* QB 159.

<sup>7</sup> Uniform Rules for Demand Guarantees (URDG, No. 458); Uniform Rules for Contract Bonds (URCB No. 524)

<sup>8</sup> *Great Eastern Hotel Co Ltd v John Laing Construction Ltd* 99 Con LR 45

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27. It is only with knowledge of the exact status of the project on a regular basis that the construction manager can deal with problems that have arisen, and therefore anticipate potential problems that may arise, and make provisions to deal with these work fronts. That is not dissimilar from the status of the Contractor under FIDIC conditions.
  28. An Employer will need accurate information of the likely completion date, and the costs, because this would affect his pre-commencement preparation and financing costs. Any change to the likely completion date would give an Employer the chance to adjust its operational dates. Judge Wilcox concluded:

*Where a completion date was subject to change the competent Construction Manager had a clear obligation to accurately report any change from the original Projected completion date, and the effect on costs.*
  29. Sub-clause (h) confirms that the Contractor has a similar obligation here.
  30. Clauses 6 and 7 deal with personnel, and with plant, materials and workmanship. Clause 6 has particular importance in relation to personnel. The Contractor must not only engage labour and staff, but must also make appropriate welfare arrangements for them.
  31. Clause 8 makes provision for Commencement, Delay and Suspension. Sub-clause 8.3 sets out the manner in which the Contractor should provide programmes showing how he proposes to execute the works. For example, the programme must be supported by a report describing the methods which the contractor is to adopt.
  32. The extension of time provisions are clear. By sub-clause 8.4:

*the Contractor shall be entitled to an extension of the Time for Completion if and ... to the extent that completion is or will be delayed by any of the following causes”.*
  33. Sub-clause 8.7 deals with delay or liquidated damages. To be able to levy such damages, the Employer must make an application in accordance with sub-clause 2.5.
  34. Clause 12 deals with measurement and evaluation. Measurement is a central feature of clause 12 and is the basis ultimately upon which payment to the Contractor is calculated. Sometimes called a “measure and value” type of contract, the arrangements in place in the FIDIC Form proceed on the basis that the Works are to be measured by the Engineer, and those quantities and measured amounts of work are then to be paid for alternatively at the rates and prices in the Contract, or else on the basis of adjusted rates or entirely new rates (if there is no basis for using or altering contract rates for the work).
  35. Clause 13 addresses variations and incorporates adjustments for changes in legislation and in costs. However, provided the Contractor notifies an inability to obtain the required goods, a variation is not binding. Equally, it is not binding in the case of contractor design if the proposed variation would have an adverse impact on safety, suitability or the achievement of performance criteria as specified.
  36. The amount the Contractor is going to be paid, and the timing of that payment, is of fundamental importance to both Contractor and Employer alike. The manner in which the payment is made is traditionally dependent on the precise wording of the contract.<sup>9</sup> Under the code of Hammurabi<sup>10</sup> the rule was as follows:

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<sup>9</sup> Although in the UK, section 109 of the 1998 Housing Grants, Construction & Regeneration Act now gives most contractors the right to payment by instalments.  
<sup>10</sup> King Hammurabi ruled the kingdom of Babylon from 1792 to 1750 BC.

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*“If a builder build a house for some one and complete it, he shall give him a fee of two shekels in money for each sar of surface.”*

37. Thus the amount to be paid was clear and given that the punishment for violating most of the provisions of the code was death, it might be presumed that most builders were paid, provided the house was constructed properly. However, the rule does not say when the payment has to be made.
38. Clauses 15 and 16 deal with termination by the Employer and suspension and termination by the Contractor, whilst clause 17 deals with risk and responsibility. This includes at sub-clause 17.6 the exclusion of the liability of both Contractor and Employer:
- for loss of use of any works, loss of profit, loss of any contract or for any indirect or consequential loss or damage which may be suffered by the other party in connection with the contract.*
39. This includes a cap on the liability of the Contractor to the Employer, something which was again new to the 1999 FIDIC form.
40. Clause 19 deals with force majeure. Whilst most civil codes make provision for force majeure, at common law, force majeure is not a term of art and no provision will be implied in the absence of specific contractual provisions.
41. Finally, clause 20 deals with claims, disputes and arbitration, and this is something, particularly in terms of Dispute Boards, with which you will be familiar.
42. So why does this paper deal with procurement and the FIDIC form? The answer to this question lies in the popularity and success of the FIDIC form. The European International Contractors have said that:
- “‘standardisation’, both in technical and diminutive matters, is more likely to result in a satisfactory and trouble-free execution of projects”.*<sup>11</sup>
43. There is no doubt that the FIDIC form is one of the more popular forms of contract, with client/employers, contractors and international financing institutions. Of course, that is not to say that the FIDIC form has been adopted wholeheartedly worldwide. The FIDIC form has not gained widespread acceptance in the United States or the UK, for example.
44. The advantage of standard form contracts, in any form of jurisdiction, is that they offer a saving in time and cost on repetitive transactions. Parties are familiar with them. With the standard form of contract, the need for negotiation and re-drafting is minimised.
45. FIDIC is also well known for its attempts to adopt an even-handed allocation of risk. For example, A. Sandberg, then head of legal services at Skanska, said of the 1999 Rainbow Suite:<sup>12</sup>

Contractors in general agree that the FIDIC Conditions of Contract have been and still are important for facilitating the tendering for and negotiating of international construction contracts. The great benefits of the present Red and Yellow Books are that the balance of risks and responsibilities as well as allocation of duties and authorities between the parties generally is accepted by both employers and contractors. The FIDIC Conditions have therefore become the baseline conditions for a fair international construction contract.

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<sup>11</sup> EIC Contractors Guide to the FIDIC Conditions of Contract for plant and design-build - ICLR (2003) Vol 20  
<sup>12</sup> A Contractor's View on FIDIC Conditions of Contract for EPC Turnkey Projects - ICLR (1999) Vol 16

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## The MDB version of the new Red Book

46. The MDB version of the FIDIC Red Book evolved out of the habit of the world's banking community of adopting the FIDIC Conditions as part of their standard bidding documents. Typically, each bank would introduce their own amendments. There were inevitable differences between these amendments and the banks realised there would be a benefit in having their own uniform conditions. This has resulted in a "harmonised edition" which was the product of preparation by the FIDIC Contracts Committee and a group of participating banks.<sup>13</sup> The first harmonised edition of the 1999 Conditions was published in May 2005, only to be amended in March 2006.<sup>14</sup> These amendments only apply to the Red Book.
47. There are a number of differences between the FIDIC form and the MDB version. One of the purposes of this paper is to consider these changes and to see how they reflect the concerns of the world banking community, particularly as reflected in the role of the World Bank itself.
48. As part of its loan package, the World Bank and the other multilateral development banks insist that recipients of aid incorporate the FIDIC terms into their tender documentation. The World Bank Procurement User's Guide makes it clear that:

*"The provisions in Section I (Instructions to Bidders) and Section VII (General Conditions of Contract) must be used with their text unchanged."*

49. In other words, the harmonised edition is not intended to replace the 1999 Red Book, except in relation to projects financed by the MDB banks.
50. The key question is whether this even-handed approach is maintained in the new Red Book, MDB harmonised edition. Remember that it is the stated aim of FIDIC to produce

*"documents which offer a fair balance of risks between the contracting parties".*

51. It can be seen that there is an immediate tension. Is it really likely that the incorporation of a number of clauses which reflect the approach of various lending institutions will maintain the "fair balance of risks" of which FIDIC is so proud? The short and simple answer to this question is that a number of the differences between the standard FIDIC Red Book and the MDB harmonised edition call into question whether or not FIDIC has been able to maintain its even-handed approach and balance between the Employer and Contractor.

52. Perhaps the most notable if not controversial changes are those to be found in clause 3 and the role of the engineer. These include the following additional clause:

*The Engineer shall obtain the specific approval of the Employer before taking action under the following sub-clauses of these conditions:*

- (a) *Sub-clause 4.12: Agreeing or determining an extension of time and/or additional costs.*
- (b) *Sub-clause 13.1: Instructing a Variation; except: (i) in an emergency; or (ii) if such a variation would increase the Accepted Contract Amount by less than the percentage specified in the Contract Data.*
- (c) *Sub-clause 13.3: Approving a proposal for variation submitted by the contractor in accordance with Sub-clauses 13.1 or 13.2.*

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<sup>13</sup> The banks involved were the African Development Bank, Asian Development Bank, Black Sea Trade and Development Bank, Caribbean Development Bank, European Bank for Reconstruction and Development, Inter-American Development Bank, International Bank for Reconstruction and Development (the World Bank), Islamic Bank for Development, Nordic Development Fund.

<sup>14</sup> There is a useful supplement prepared by FIDIC to the MDB version which acts as a user's guide. This includes a section on Changes to the Construction Contract General Conditions.

(d) *Sub-clause 13.4: Specifying the amount payable in each of the applicable currencies.*

53. Further, whilst under the 1999 edition, “*The Employer undertakes not to impose further constraints on the Engineer’s Authority, except as agreed with the Contractor.*” Under the MDB version, this is replaced with: “*The Employer shall promptly inform the Contractor of any change to the authority attributed to the Engineer.*”
54. Perhaps the first of these changes is the most controversial. Under the 1999 edition, the Employer actually undertook not to change the basis of the Engineer’s authority without the agreement of the Contractor. This has been changed to give the Employer the right to make whatever changes it likes to the basis of the Engineer’s authority. The only restriction is that it must inform the Contractor of these changes. There is no longer any requirement that the Contractor agrees to these changes. Whereas the second change might be viewed as fettering the Engineer, particularly in the fact that the new clause says that the Engineer cannot agree or determine any extension of time or cost consequence of said extension without the Employer’s approval.
55. The view of contractors is that this is a retrograde step permitting unilateral alteration of the Engineer’s authority, and thus potentially impacting upon the balance of risk.<sup>15</sup> Accordingly, it is likely to impact upon the way in which potential contractors tender for the project.
56. There are a number of other similar features within the MDB version.<sup>16</sup> The impact of some of these is obvious but sometimes, the point is not so clear at first glance. These include apparently simple changes such as the change from the 1999 Red Book’s “reasonable profit” to “profit”. By sub-clause 1.2(e) that profit is fixed at 5% unless otherwise agreed. From a funder’s point of view, the purpose of the change is a clear one; everyone knows what the Contractor’s profit is. Some might argue that 5% is a little low, or at least not reasonable.
57. Under clause 2.5 of the 1999 FIDIC Red Book, the Employer is now required to give notice of his claims “as soon as practicable” after the Employer becomes aware of any event which gives rise to a claim. Whilst this is far from as onerous as the condition precedent, 28-day limit placed on the Contractor by clause 20.1, it is a new requirement of the 1999 form and could be said to be an example of the balance FIDIC is looking for.
58. However, under the MDB harmonised version, the following change has been introduced to the sentence which details when the Employer must give notice. The sub-clause now reads as follows:
- The notice shall be given as soon as practicable *and no longer than 28 days* after the Employer became aware, *or should have become aware*, of the event or circumstances giving rise to the claim. A notice relating to any extension of the Defects Notification Period shall be given before the expiry of such period.
59. The first impression given by the addition of the underlined words is that they serve to tighten up the period in which the Employer must notify any claim an impression reinforced by the apparent 28-day time limit. However, the new words introduce an additional subjective reasonableness test. Whereas before, all that mattered was when the Employer actually became aware of the circumstances giving rise to a claim, now some consideration needs to be given to when the Employer should have realised that a claims situation had arisen. However, in

<sup>15</sup> Appuhn, R. and Eggink, E, *The Contractor’s View on the MDB Harmonised Version of the new Red Book* (2006) ICLR 4.

<sup>16</sup> Not all the differences are set out in this paper.



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reality, save for extreme cases, little has changed. There is still no time limit to serve as a condition precedent to deprive the Employer of the opportunity to make a claim.

60. In sub-clause 4.2, the four circumstances under which an Employer is entitled to make a call under the performance security have been deleted. There is no equivalent replacement and now the Employer is able to make a call in respect of amounts to which it is entitled under contract. Arguably, this represents an extension of the Employer's rights and may make it easier for the Employer to make a call under the performance security, although it might have been felt that the reference to the ICC Uniform Rules provides an adequate safeguard for the Employer, the financing institutions and the Contractor.
61. The amendments to sub-clause 4.12 have had an interesting history. Sub-clause 4.12 provides that a Contractor may be entitled to an extension of time in respect of unforeseeable physical conditions. Under the May 2005 version of the MDB harmonised edition, sub-clause 1.1.6.8 defined unforeseeable as meaning:

*“Not reasonably foreseeable and against which adequate preventative precautions could not be taken by an experienced contractor by the date for the submission of the Tender”.*

62. This was a controversial amendment. The European International Contractors Group criticised the addition, referring to it as a *“twist of Catch-22 proportions”*<sup>17</sup> and the editors of the *International Construction Law Review* indicated that the change calls for:

*“rational justification and explanation of its practical application”.*<sup>18</sup>

63. It could be argued that the addition to the clause serves to add clarity to the original definition, no more. For example, in demonstrating that the physical conditions would have been unforeseeable to an experienced contractor, the Contractor would already have to show that there were no adequate precautions which could have reasonably been taken. However, the EIC raised three questions of the amendment:

- (i) Is it the intention that contractors should make allowances for precautionary steps for unforeseeable events and circumstances?
- (ii) Is it the intention of the MDB harmonised edition to shift the balance of risk under the contract for unforeseeable events to the contractor?
- (iii) How can you take reasonable precautions against an event which is not reasonably foreseeable?

64. The answer to the first question does appear to be yes, which may well have an impact on the tender returns. If the answer to the second question is yes then this would suggest that the contract drafters are moving towards the risk profile adopted under the Silver Book. A simple comparison between the two forms of wording seems to make it clear that this is not the intention behind the new clause.

65. It was the third question which demonstrated the real difficulty with the new wording and this may have been one factor which led to the revision being dropped. However, as there have been two versions, care should be taken to check which definition has been adopted.

66. The position of clause 6 is an interesting one. Clause 6 deals with the workforce and places a wide responsibility onto the shoulders of the

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17 Appuhn and Eggink, “The Contractor’s View on the MDB Harmonised Version of the New Red Book” in *International Construction Law Review* (2006) 4

18 “Introduction” *International Construction Law Review* (2006) 23 (January)

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Contractor. This clause reflects the international flavour and the type of projects for which FIDIC contracts are often used. In particular, with overseas projects where the Contractor may employ staff from his own country and also where those projects are in remote locations (for example process plants), this provision of welfare is key. The Contractor will therefore need to allow for such provision in his tender and take into account, in doing so, the particular location of the works and the difficulties that might be encountered in making arrangements for payment (e.g. local currency conversion), housing (e.g. location), feeding (e.g. local laws/religious customs) and transport (e.g. local infrastructure).

67. Although the Contractor's prima facie responsibility extends to local staff and labour, in engaging local staff and labour the Contractor should also be aware of local labour laws (which may not be the same as the law governing the Contract) and, in particular, aspects of that law which might conflict with the obligations of the Contract (see below). Where problems such as this arise, the Contractor will have to ascertain whether he can "contract out" of local, conflicting labour laws or whether he is bound by them. In either case, the ensuing risk must be built into the Contractor's price for the Works.
68. The Guidance provided in the 1999 edition for the preparation of Particular Conditions, sets out some examples of sub-clauses that can be added to clause 6 to take account of particular circumstances and the locality of the site. These, for example, cover matters such as the provision and importation of foreign staff and labour, measures against insect and pest nuisance, alcoholic liquor and drugs, arms and ammunition, and festivals and religious customs.
69. The new MDB harmonised edition FIDIC form includes 10 of these "particular locality" clauses as part of the General Conditions. The reasons for the adoption of these clauses have nothing to do with concerns about financial security. They reflect the concern of the world banks about the welfare, health and safety of the local workforce. For example, the following additional paragraph has also been included as part of 6.1:

The Contractor is encouraged, to the extent practicable and reasonable, to employ staff and labour with appropriate qualifications and experience from sources within the Country.

70. This is self-explanatory and like a number of the other amendments reflects a desire on the part of the World Bank to encourage local enterprise.<sup>19</sup> However, as it happens, one likely impact of these clauses is to increase the administrative burden placed upon the Contractor, and hence the cost. For example, sub-clause 6.22, which deals with the employment records of workers, requires that a contractor keep

*"complete and accurate records of the employment of labour."*

The records must include:

*"the names, ages, genders, hours worked and wages paid to all workers.  
These records shall be summarised on a monthly basis and shall be available for inspection"*

That is a higher administrative burden that can be found on contracts in the UK.

71. The changes to sub-clause 12.3 are pro-Employer. Sub-clause 12.3 sets out circumstances when the Contractor can claim enhanced rates. In the

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<sup>19</sup> See for example sub-clause 4.4

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MDB version, the rates shown in sub-paragraphs (a)(i) and (ii), which can trigger the use of rates other than those specified in the Contract, have been increased from 10% and 0.01% to 25% and 0.25% respectively. This seems to be a pro-Employer change as the increase in the threshold amount is of no benefit to the Contractor.

72. Some clauses in the MDB version are entirely new. One such is 15.6 which deals with corrupt or fraudulent practice. Sub-clause 15.6 states that:

If the Employer determines that the Contractor has engaged in corrupt, fraudulent, collusive or coercive practices, in competing for or in executing the Contract, then the Employer may, after given 14 days notice to the Contractor, terminate the Contractor's employment under the Contract and expel him from the Site, and the provisions of Clause 15 shall apply as if such expulsion had been made under Sub-Clause 15.2 [Termination by Employer].

Should any employee of the Contractor be determined to have engaged in corrupt, fraudulent or coercive practice during the execution of the work then that employee shall be removed in accordance with Sub-Clause 6.9 [Contractor's Personnel].

For the purposes of this Sub-Clause:

See Notes for definitions of corrupt, fraudulent, collusive or coercive practices for each Participating Bank.

73. The sub-clause will be slightly different for each Participating Bank as each has its own definition of corrupt, fraudulent, collusive or coercive practice. The sub-clause has some similarities with sub-paragraph (f) of sub-clause 15.6; however, unlike sub-clause 15.1(f), here 14 day's notice must be given. This new sub-clause is also more widely drawn, for example making it clear that the tendering process must be fair as it refers to both "competing for" and "executing" the Works. In the case of *Cameroon Airlines v Trasnet Ltd*,<sup>20</sup> an arbitration tribunal ruled that Trasnet had to repay commission monies it had added to its tender sum the commission monies being money paid as bribes to officials.
74. This extension to clause 15 is entirely in keeping with the global trend in seeking to clamp down on this type of behaviour. For example, in the UK, the Anti-Terrorism, Crime and Security Act 2001<sup>21</sup> provides that a UK citizen can be guilty of an offence in the UK if he is involved in offering or receiving bribes abroad, provided that what he has done would amount to an offence in the UK.
75. The World Bank is always analysing ways to bolster up its anti-corruption activities. This will include a review of the sanctions reform process and a possible expansion of its investigative role.
76. Sabotage has been added at sub-clause 17.3 as an Employer risk item. Under sub-clause 17.6, the sub-clause has been extended to make it absolutely clear that certain items, for example delay damages, are not covered by the limitation of liability provisions.
77. However, the story is not entirely one-sided. Not every change is pro-Employer. Take, for example, sub-clause 4.2. As stated above, under the standard form, clause 4.2 provides a mechanism whereby the Contractor can obtain confirmation that sufficient funding arrangements are in place to enable him to be paid. Under the MDB harmonised edition, there have been a number of changes. First, the Employer must submit reasonable evidence of its financial arrangements before the project commences in other words the Contractor does not have to request it. This seems to be pro-Contractor. However, there has been a

20 [2004] EWHC 1829

21 Thereby adopting the 1999 Organisation for Economic Co-operation and Development Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.

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further more subtle change. Under the standard form, the Employer has to give notice if it “intends to make” any material change to his financial arrangements. Under the MDB version, that notice only has to be given “before the Employer” makes the change. This would have the effect of pushing back the time that an Employer needs to inform a Contractor of any such change.

78. Finally, the MDB version of the clause requires an Employer to notify the Contractor within seven days if a bank has suspended payment of any loan which may be financing the project. This therefore gives the Contractor some early warning of potential financial problems with the project, something which he does not have under the FIDIC standard form.
79. In similar vein, under sub-clause 8.1, the project cannot commence until the contract agreement has been signed by both parties, the Contractor has reasonable proof that the Employer can fund the works and the Contractor has received any advance payments it was entitled to. The condition is stated to be condition precedent and the Contractor is given the option of terminating the contract if no instruction is received.
80. In addition, the threshold as to when any repayment of the advance payment (if any) must be made has been increased from 10% of the Accepted Contract Amount to 30%, a more contractor-friendly change.
81. The position of the Contractor is also improved by the provisions made by sub-clause 14.9 for the use of retention bonds in respect of the second half of retention after the issue of the Taking Over certificate.
82. Limits have been imposed on the Employer’s right to terminate at his own convenience. This should prevent the Employer from acting pre-emptively, if it considers that the Contractor is poised to determine.
83. So where does that leave the MDB harmonised contract form. It will be clear from the above that there have been two editions of the MDB conditions issued within a short time of each other, suggest that they were not quite right initially. It was also perhaps inevitable, given the fact that the conditions derive from a particular source with a particular pro-employer interest, that the conditions are certainly viewed by the contractors as being of an “employer-friendly” nature. However, the fact remains that in terms of procurement on World Bank funded projects, the adoption of the MDB harmonised form is a mandatory requirement.

## Procurement and the World Bank

84. You cannot ignore the role of the World Bank in international procurement. One of its primary purposes is to make loans, at low affordable interest rates, to developing countries. Indeed, if the developing countries cannot afford a loan, the bank will make grants. Note that commercial banks will not generally lend to projects in countries that have rescheduled their debts or are perceived to be about to reschedule. Often these grants and loans are used to fund infrastructure projects. Typically, the way the World Bank operates is to agree to make a loan in advance. The loan account will then remain open for a fixed period. More often than not, these infrastructure projects will be carried out by major contractors and consultants, either themselves or in joint ventures with local parties.
  85. Whilst the role of the bank might stretch to insisting that specific procurement documentation is used, the World Bank will not administer
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contracts itself. In other words, the World Bank will lend money, but not necessarily intervene if the contractor or consultant is having problems getting paid. Their view is that any attempt to influence the payment process could result in the bank being dragged into the middle of contractual disputes. The bank does not have the mandate nor, to be fair, the resources to undertake this.

86. In the view of the Bank, many payment problems are caused by the use of lump sum contracts associated with weak supervision, although these contracts do offer the advantage of not rewarding poor performance for delays in execution.
87. The World Bank has its own procurement rules. As made clear above, the World Bank, along with other development banks, as part of their loan packages, insists upon the use of its own standard package of documents for the procurement projects. This package is known as the Standard Bidding Documents for Procurement Works (“SBDW”). The Standard Bidding Documents for Works, otherwise known as the SBD-W, have been prepared by the World Bank for use by borrowers in the procurement of works through international competitive bidding. *The User’s Guide for the Procurement of Works* notes that an important feature of the SBD-W is that it can be used with minimum changes.<sup>22</sup>
88. The World Bank also produces a *User’s Guide for Procurement of Works*. The most recent is dated March 2007. Copies of these documents can be found on the World Bank website [www.worldbank.org](http://www.worldbank.org). The SBD-W contains its own standard form of contract terms, being an amended version of the 1999 FIDIC Red Book and the Red Book only. The Red Book, as stated above, is used for civil engineering or building works that are to be designed by the employer.<sup>23</sup>
89. The World Bank is clear that: *“The SBD-W must be used for the procurement of works contracts financed in whole or in part by the Bank unless the Bank agrees to the use of other bidding documents acceptable to the Bank.”*
90. The SBD-W notes that the use of the Conditions of Contract for Construction for Building Engineering Works Designed by the Employer, Multilateral Development Bank Harmonized Edition, prepared by FIDIC, is compulsory. The User’s Guide makes it clear that: *“The provisions in Section I (Instructions to Bidders) and Section VII (General Conditions of Contract) must be used with their text unchanged.”*
91. The User’s Guide to the Bidding Process sets out the following stages:
  - (i) Publicity: advertising or notice
  - (ii) Preparation and issuing of bidding documents
  - (iii) Bid preparation submission
  - (iv) Bid opening
  - (v) Bid evaluation
  - (vi) Contract award.
92. For World Bank projects, the employer must remember that it is a mandatory requirement for them to use the standard bidding documents issued by the Bank for any contracts financed by the Bank. It is the potential employer who is responsible for the preparation and issuing of the bidding documents. They must use the published version of the

<sup>22</sup> Many of the features of World Bank procurement are of course equally applicable to many other forms of procurement.

<sup>23</sup> See clause 4.1.

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SBD-W without suppressing or adding text to any of the sections.

93. A potential employer must advertise any upcoming bidding processes in at least one newspaper of national circulation, official gazette or electronic portal with free access, in the borrower's country. Any invitations to tender must also be published in the UNDBonline (UN Development Business on line) and the dgMARKET. Notification must be given in sufficient time to enable prospective bidders to obtain pre-qualification or bidding documents and prepare their responses.<sup>24</sup>
94. The World Bank considers that not less than six weeks from the date of the invitation to bid is the minimum appropriate time to allow tenderers to prepare a bid. Where large works or complex items of equipment are involved, this period should be extended to a minimum of 12 weeks. As with any large project, the World Bank recommends that site visits are arranged where appropriate. The World Bank also requires that employers respond promptly to requests for clarification from bidders and amend, as may be required, the bidding documents.
95. The employer is, as you would expect, responsible for the bid opening. Care must be taken at such an event lest the process has to be cancelled and started again.<sup>25</sup>
96. In relation to the bid evaluation, the World Bank advises the following:
  - (i) the appointment of experienced staff to conduct the valuation of the bids;
  - (ii) keeping the bid evaluation process strictly confidential;
  - (iii) rejecting any attempts or pressures to distort the outcome this includes fraud/corruption;
  - (iv) always complying with the requirements of the World Bank; and
  - (v) applying "only and all" of the criteria specified in the bidding documents.
97. The standard format for the invitation for bids includes the statement that qualified domestic bidders may be eligible to receive a margin of preference of 7.5% bid evaluation.
98. Any evaluation of a bidder's technical proposal must include an assessment of the bidder's technical capacity to mobilise key equipment and personnel for the contract, taking into account its proposals regarding methods, scheduling and sourcing of materials. Other issues that will need to be considered are:
  - (i) experience
  - (ii) financial situation
  - (iii) current contract commitments
  - (iv) cash-flow capacity
  - (v) allocation of equipment
  - (vi) personnel
  - (vii) time for completion
  - (viii) pending litigation.

<sup>24</sup> See paragraph 8 of the World Bank guidelines.

<sup>25</sup> Note that the term "bid opening" must be used with caution. For example, a bid for which a bid withdrawal or bid substitution notice was received on time shall not be opened, but returned unopened to the bidder in question. Thus, the sequence in which bids are handled and opened is crucial.

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99. A domestic bidder, for an individual firm, is one registered in the country of the borrower which has more than 50% ownership by nationals of the country of the borrower and does not subcontract more than 10% of the contract price to foreign contractors. A domestic joint venture must be registered in the country of the borrower and must satisfy the requirements set out as for individual firms.
100. In relation to financial resources, a bidder will need to demonstrate that it has sufficient construction cash-flow for the number of months the project will run, taking into account the time needed by an employer to pay an invoice. A bidder must demonstrate access to/availability of adequate financial resources, be they liquid assets or lines of credit.
101. When it comes to the suitability of key personnel, what matters is a minimum number of years of experience in a similar position or on a comparable project. The World Bank guidelines note that the requirement of specified education and academic qualifications is normally unnecessary for such positions. The World Bank is well aware that many competent staff have learned their profession on the job, rather than through academic training.
102. When it comes to the evaluation and qualification criteria, the key is that bidders are:
- qualified by meeting pre-defined, precise minimum requirements ... For that purpose, clear-cut, fail-pass qualification criteria need to be specified in order to enable bidders to make an informed decision whether to pursue a specific contract and, if so, either as a single entity or in joint venture. The criteria adopted must relate to characteristics that are essential to ensure satisfactory execution of the contract, and must be stated in unambiguous terms.<sup>26</sup>*
103. That is not unusual and is entirely in keeping with the principle of the equal treatment of tenderers. In short, this principle requires that all tenders comply with the tender conditions so as to ensure an objective comparison of the tenders submitted by the various tenderers. This concept recently came before the European Courts in the case of *EMM G Lianakis AE and Others v Municipality of Alexandroupolis* (Case C-532/06).
104. This was a case about Article 36(2) of Council Directive (EEC) 92/50 which provides that:
- Where the contract is to be awarded to the economically most advantageous tender, the contracting authority shall state in the contract documents or in the tender notice the award criteria which it intends to apply, where possible in descending order of importance.*
105. Here, the town council had invited tenders for a town planning project. It had set out the award criteria in the contract notice and had listed these criteria in a specific order of priority. The list was (i) proven experience on projects carried out over the last three years (ii) manpower and equipment and finally (iii) the ability to complete the project by the anticipated deadline. Thirteen consultancies responded. However, during the evaluation procedure, the committee in charge of the appointment set weightings of 60%, 20% and 20% for each of the three award criteria. It also set up certain sub-criteria, for example stipulating that experience should be evaluated by reference to the value of completed projects.
106. As the stipulation of the weighting factors and sub-criteria were only made at a date after the submission of the tenders, certain tenderers brought proceedings against the town council. The Greek Court referred

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<sup>26</sup> See section (iii) of the World Bank User's Guide for procurement of works.

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the case to the European Court, asking whether Article 36(2) precluded a contracting authority from acting in this way, i.e. stipulating at a later date the weighting factors and sub-criteria to be applied to the award criteria referred to in the contract documents or notice.

107. The European Court noted that the purpose of the legislation is to ensure that there is no discrimination between different service providers. Where a contract is to be awarded to the economically most advantageous tender, a contracting authority must state in the contract documents the award criteria that it intends to apply. Potential tenderers must be in a position to ascertain the existence and scope of the criteria elements when preparing their tenders. Therefore, a contracting authority cannot apply weighting rules or sub-criteria that it has not previously brought to the tenderers' attention.
  108. Tenderers must be placed on an equal-footing throughout the procedure, which means that the criteria and conditions governing each contract must be adequately publicised by the contracting authorities. Here, the projects award committee referred only to the award criteria and it was only later after submission of the tenders that it introduced the stipulation of the weighting factors. Accordingly, this did not comply with the article requirements.
  109. In other words, the European Court was making clear that compliance with the legislation requires the equal treatment of tenderers. The evaluation process must be transparent and objective. That had not happened here.
  110. As to the consequences of any such breach? Well, where a public authority does not adhere to applicable public procurement law (colloquially the "OJEU Procedure") when tendering for work then it is susceptible to a claim by an aggrieved tenderer. The whole thrust of the public procurement law is to ensure that those tendering are able to compete on an equal basis and that public contracts are awarded fairly. It is perhaps less well known that in addition to the OJEU Procedure, there is common law authority to the effect that public authorities engaged in tendering processes may in fact create collateral contracts with the tendering parties. The nature of those contracts is likely to be that if the public authority in question has stated that it will evaluate tenders in accordance with a given procedure, then that public authority is obliged to the tendering parties to do just that.
  111. There are also some interesting comments to be found in the [User's Guide](#) about the bill of quantities. The guide notes that:
    - the objectives of the Bill of Quantities are
      - (a) to provide special information on the quantities of Works to be performed to enable bids to be prepared efficiently and accurately; and
      - (b) when a contract has been entered into, to provide a priced Bill of Quantities for use in the periodic evaluation of Works executed.
  112. The best way to achieve these objectives is to itemise the works in sufficient detail.
  113. A daywork schedule should only be included if the probability of unforeseen work outside of the items included in the bill of quantities is relatively high. The daywork schedule should comprise a list of the various classes of labour, materials and equipment for which basic daywork rates or prices are to be inserted, together with a statement of the conditions under which a contractor will be paid for work executed
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on a daywork basis. In addition, a tenderer should enter a percentage against the basic daywork subtotal amount representing profit, overheads, supervision and other charges. With dayworks, work must not be executed on a daywork basis except by written order.<sup>27</sup>

114. The World Bank User's Guide tries to deal with the difficulties of provisional sums by noting that specific provisional quantities should be entered against items and a tenderer should not deal with these issues merely by increasing the quantities for a class of work beyond that normally expected to be required.
115. It is expected that the rates and prices bid will include all plant, labour, supervision, materials, erection, insurance, profit, taxes and duties.<sup>28</sup> That is, unless stated otherwise.
116. The World Bank also recognises the potential costs of the "particular locality" or "social clauses" to be found within the MDB harmonised version of the FIDIC form, as discussed above. The potential employer is required to decide on a case-by-case basis whether these costs are to be considered by the bidder as part of its overhead or as an item of cost associated with one or more of the items within the bill. The general rule is that such costs should be part of the bidder's overhead unless the cost to comply would represent a large component of the works. In any event, the prices used must not be lump sums as it is important that the facilities are measured and paid through monthly instalments in order that supervision and control of the necessary facilities and services can be maintained.
117. The World Bank User's Guide gives two examples. Sub-clause 6.7 has specific regard to HIV/Aids prevention. Where a government has public programmes in place for HIV/Aids, it is likely that a contractor would only need to create a support basis the costs of which can and should be included in its overhead. However, the costs of accommodating workers in remote locations may well be of a much higher value and so should be treated differently.
118. One special item to note is the prohibition on child labour. This is particularly important to the World Bank and specific note is made of sub-clause 6.21 in the User's Guide with reference to Article 1 of the Convention of the Rights of the Child adopted by the UN General Assembly in November 1989 which states: "*a child means every human being below the age of 18 years unless the law applicable to the child, majority is obtained earlier*".
119. The MDB worked with FIDIC to harmonise the wording of the clauses and the various amendments which appeared in the conditions special to each of the banks. It is important to note that the harmonised edition is not intended to replace the 1999 Red Book. It is there to standardise the varying provisions that have been included by the various multilateral development banks.
120. It is important to remember that the MDB harmonised edition of the FIDIC contract, has been prepared for a measurement type of contract and should not be used, without major modifications, for other types of contract, e.g. design and build. The standard text must be used in its entirety. One reason for this is to ensure a high degree of reading, understanding and interpretation by all concerned, including bidders and the banks. The World Bank says:

the use of standard conditions of contract for all civil Works will ensure comprehensiveness of coverage, better balance of rights or obligations

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<sup>27</sup> See sub-clause 13.6 of the general conditions of contract.

<sup>28</sup> This will include all risk and liabilities.

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between Employer and Contractor, general acceptability of its provisions, and savings in time and cost for big preparation and review, leading to more economical prices.

121. So is the World Bank suggesting that in time familiarity will achieve the balance which is the stated aim of the FIDIC Board? This is perhaps being a little disingenuous as the MDB harmonised edition has essentially been modified at the request of and to meet the requirements and needs of the world banks. Until such time as familiarity has this effect, remember that contractors will respond to any perceived imbalance of risk by pricing accordingly.

## Conclusion

122. World and MDB Bank projects are typically in developing countries. Therefore it is worth considering some of the risks that will typically be encountered, risks which potential tenderers, be they JV or otherwise, would do well to bear in mind. A major factor is political risk. This can be a major factor in developing countries and can add significant costs to the project. Typically, the host state will be involved, at least indirectly. Thus, the project cannot be treated simply as an ordinary commercial development. There will be an intermingling of commercial, legal and political considerations.
123. Indeed, does the project require government authorisation or at least state cooperation and support during operation? The government or its agencies will often be in a position to revoke authorisations, impose new taxes and even nationalise or expropriate the project. Is the institutional structure sufficiently clear, such that the relevant authorities can be identified and a decision or authorisation obtained which will bind the necessary authorities? Is the project one which is in tune with overall government policy and likely to be promoted?
124. Political risks vary, but include the following:
- (i) Nationalisation;
  - (ii) Confiscation or ex-appropriation, with or without compensation;
  - (iii) Currency devaluation<sup>29</sup> or adverse changes in exchange control regulation;
  - (iv) Import restrictions/quotas on fuel or equipment;
  - (v) Higher or selective taxes, duty or withholdings;
  - (vi) Political instability following changes in government;
  - (vii) Disputes between state and local governments or between government departments;
  - (viii) Corruption;
  - (ix) Risk of violence against expatriates and civilians;
  - (x) Cross-border risks restrictions on export licences for equipment or technology/blockades or embargoes; and
  - (xi) Land ownership issues particularly if there has been a recent war.
  - (xii) Must authorisation for the employment of foreigners be obtained? Will it be revoked?

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<sup>29</sup> Many countries have currencies that are not generally regarded as stable over the long term. There may be a differential between official and market rates for conversion of the local currency to hard currency.

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125. Political risk insurance cover is available, although the cost is often high.
126. Agreements with government entities sometimes raise issues of validity and enforceability. Of these issues, the capacity of the relevant entity to enter into agreements and its potential rights to claim sovereign immunity from them are crucial. Individuals who negotiate and sign agreements must have the capacity to bind the government (or other) body that employs them. The government body with whom agreements are made must have the legal right to enter into the agreements. There must always be a clear understanding of exactly how far such capacity extends and if there are any limitations on the powers of the individuals and bodies concerned. In some jurisdictions (for example Saudi Arabia), government entities are prohibited from entering into arbitration agreements. Any project should be implemented under a transparent, certain and enforceable legal framework. There must be a clear policy and implementation process.
127. Insurance must also be checked. Are there statutory levels of cover? Is the concept of co- insured beneficiaries recognised? What about subrogation? What authorisations are required in relation to insurance policies? What about the use of offshore insurers? Reinsurance?
128. What about the environment? Are environmental impact statements or consents/authorisations required? What are the penalties for non-compliance? What is the relevant regulatory authority? Is the project site in a specifically/specially protected area?
129. The importance of preparing the legal framework should not be underestimated. The introduction of a specific legal framework is to permit projects, together with a consistent and coherent legal basis for foreign investment, is a very important step.
130. However, ultimately, any major international project will involve an assessment of the risks involved. The final factor in assessing risks is the question of mitigation. Therefore it is imperative that you consider:
- (i) The substantive effect of the local law;
  - (ii) The clarity of local laws and interpretation of contracts governed by local law;
  - (iii) The quality, reliability, independence and impartiality of the local courts; and
  - (iv) The enforceability of foreign judgments or arbitral awards through the local courts.
131. Accordingly, the advice of a local lawyer can be invaluable.

Jeremy Glover  
28 February 2008

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